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ONOMIC SITUATION IN
SOUTHERN CHINA

On April 1, 1961, General George F. Kennan, Director of Intelligence Research, Institute of World Politics; the Honorable L. R. Gandy, Director for Intelligence, Department of the Army; the Honorable John C. Stennis, Chairman, U.S. Senate Select Committee on Intelligence; General James A. Schlesinger, Director of Defense Intelligence Agency; General John H. Hall, the Director to the Chairman of the Joint Chiefs of Staff; General John D. Nichols, Director of the Defense Systems Management Organization; and the Director of the Defense Electronic Systems Organization, the Defense Control Commission, participated in a discussion on the situation in South Vietnam. The discussion was conducted in an informal, unclassified, and non-technical manner.

trial production is likely to increase about 12 percent annually, as compared with about 33 percent in 1959 and 16 percent in 1960. (Paras. 31-35)

4. If 1961 is another poor crop year the economic and political effects for Communist China are likely to be grave. There probably would be no increase in gross national product (GNP) in 1961, and growth prospects for later years would also be affected. Unless there were substantial food imports, malnutrition and disease would become widespread, and a considerable amount of starvation probably would occur. Public disaffection probably would become a major problem for the regime, perhaps forcing it to

undertake a massive campaign of threats and terror. It is unlikely even in these circumstances, however, that public disaffection could threaten continued control of China by its present leadership. (Paras. 38-40)

5. We do not believe that Peiping would accept food offers from the US even under conditions of widespread famine. (Para. 42)

6. We do not believe that even famine conditions would, in themselves, cause Peiping to engage in direct military aggression. Such difficulties probably would, however, prompt Peiping to avoid actions which would exacerbate its relations with Moscow. (Paras. 40-41)

DISCUSSION

I. INTRODUCTION

7. The Chinese Communist regime is now facing the most serious economic difficulties it has encountered since 1949-1950. As a result of two successive years of poor harvests, the withdrawal of Soviet technicians, and the dislocations created by the "Leap Forward," the Chinese leaders have been forced sharply to slow down the pace of the country's economic development program.¹ The most acute of these problems is the food shortage: the output of grain in 1960 has dropped to about the 1957 level, when there were an estimated 50 million fewer Chinese to feed. This situation has increased popular discontent and apathy and weakened party morale.

II. COMMUNIST CHINA'S ECONOMIC DIFFICULTIES

The Agricultural Crisis

8. Peiping's orthodox Communist program for economic development has been based on the belief that China could be industrialized rapidly, despite its technological backwardness and the unfavorable ratio of population to arable land. Consumption was to be held in check and industrial plant was to be built up with technical assistance and large-scale imports of machinery from the USSR. Agriculture, which had the threefold task of: (a) feeding a fast-growing population; (b) supplying increasing quantities of raw materials to industry; and (c) providing goods for export, was to rely primarily on labor-intensive projects and programs. The modernization of agriculture was to wait until industry developed enough to provide simultaneously the resources for further industrial growth and for increased investment in agriculture.

This program involved a deliberate gamble that the thin margin between the production of food and the minimum needs of the population could be maintained. There are growing indications that Chinese leaders now realize that this gamble has not succeeded.

9. Agricultural production, which had barely kept ahead of population growth until the past two years, has now dropped behind. The situation has become especially acute as regards foodgrains, which make up 85-90 percent of the Chinese diet. Although foodgrain production increased by an estimated 10 percent—from 168 to 185 million metric tons—during China's First Five-Year Plan (1953-1957), this was more than offset by the estimated 12 percent population increase, and only a slightly more rapid growth of other foods made possible a small improvement in the people's diet.¹ The situation was temporarily eased by a bumper crop in 1958, when foodgrain production reached an estimated 212 million tons. During late 1958, however, the regime allowed food to be consumed through free supply in the commune mess-

¹All figures on grain production are in metric tons of unhusked grain, and include the grain equivalent of tubers.

The statistics used in this SNIE for agricultural and industrial production are only approximations. The Chinese Communists have made it difficult for foreign observers to use official data in gaining a clear understanding of the workings of the economy. At the present time, moreover, there is much less official information than would ordinarily be available on 1960 performance and the 1961 plan. Official statements about economic trends in 1960 and early 1961, however, tacitly support the general conclusions of this SNIE. Official statements have hinted that production of basic food crops was close to the level of production in 1957. With the exception of a few industrial commodities, industrial output is admitted to have fallen short of the 1960 targets.

The population figures used in this estimate are based on the official census figures for 1953 together with scattered official data on birth rates and death rates, and with comparisons with similar Asian cultures.

Although the scarcity of data for 1960 precludes making precise estimates of population, production of food crops, and production of many important industrial commodities, the data are believed adequate to support the year-by-year trends and general conclusions of this SNIE.

halls at a rate that it could not sustain. By early 1959 food reserves were already low and local shortages had appeared in many areas of the country.

10. Since 1958 the problem has been greatly intensified by two consecutive poor crop years. Foodgrain production in 1959 declined to an estimated 190 million tons, and the 1960 harvest is estimated to have been only 180-190 million tons. Moreover, the quality of the Chinese diet has declined: consumption of foods rich in nutrients, such as meat, vegetable oils, and soybean products, has fallen. Thus, a very low per capita caloric intake has been sustained for nearly two years despite the heavy labor demands on the Chinese people.

11. Widespread famine does not appear to be at hand, but in some provinces many people are now on a bare subsistence diet and the bitterest suffering lies immediately ahead in the period before June, when the first 1961 crops will be harvested. Serious diseases of malnutrition, such as beri-beri and nutritional edema, are widespread in the worst hit areas of the country. In addition, the lack of food has increased the incidence of other types of diseases, such as tuberculosis and liver trouble. Many workers apparently are so weakened by lack of food that normal workloads cannot be performed.

12. Although firm information is lacking, non-food crops also experienced a poor year in 1960. The important cotton crop is estimated to have been less than in 1959, temporarily halting growth in the textile industry and bringing on an even stricter rationing of cotton cloth. Production of oil-seeds and soybeans in 1960 probably was no higher than in 1959 and may have been somewhat lower.

13. The recent failures of Chinese agriculture have been due principally to adverse weather conditions. It is clear that 1959 and 1960 were years of severe natural disasters in China. In 1960, most of the major wheat-growing areas in North China were affected by severe and extended drought. In rice growing areas of the Yangtze Valley and South China weather was average in 1960, and rice

production was about the same as in 1959. However, some areas in the south were subjected to typhoons and floods which caused severe local rice shortages.

14. Bad as the weather was in 1959 and 1960, the regime appears to have been deliberately exaggerating the scope of weather difficulties in order to shift blame from itself. Some of the agricultural difficulties of the past two years have resulted from excesses and mismanagement attending the "Leap Forward" and the commune programs: the disruptive effects of commune reorganizations, vacillating policies with respect to private plots and private livestock holdings, the drive to grow more on less land, and agricultural innovations that ignored practical experience and could not be quickly assimilated under varying local conditions.

15. Peasant fatigue and apathy have also played a part. The people have been overworked for three years, their lives regimented, and they have been forced to do much work which they have felt was wasted. Finally, there have been no material rewards to compensate for the extra demands placed on them by the regime.

Sino-Soviet Economic Relations

16. The deterioration of political relations between Communist China and the USSR during 1960 further compounded Peking's economic difficulties. In July-August the USSR abruptly withdrew all or nearly all of the [redacted] Soviet industrial technicians in Communist China. The removal of these technicians has retarded the schedules for the installation of equipment and the opening of some new plants, and probably has caused the temporary cancellation of other projects.

17. The withdrawal of technicians has been the major economic sanction applied by Moscow during the period of China's open challenge to Soviet authority in the Bloc. China's short-term indebtedness to the USSR during 1960 increased [redacted] one of several indications that the USSR did not ex-

tend its economic pressure to the point of curtailing the general flow of commodities to China. Nevertheless, the withdrawal of the technicians and the cooling of political relations probably caused some disruption in Sino-Soviet trade.

18. The explanation for the shortages of petroleum products in late 1960 is unclear. These shortages have affected aircraft and military activities, truck distribution of food, and passenger transport in major cities. In previous years the USSR acted quickly to make supplementary deliveries of petroleum products when the shipments provided for in the annual trade agreement were not sufficient to last through the year. No supplementary supplies were forthcoming in 1960, although current deliveries are apparently normal. The shortage in late 1960 may have been due to Chinese reluctance to request supplementary supplies at a time of political tension and trade difficulties, or the Chinese may have sought additional supplies but were turned down by the USSR.

Demise of the "Leap Forward"

19. During 1960 it became increasingly apparent that the "Leap Forward" was in fact ending and that Peking recognized it could not continue the breakneck industrialization tempo of 1958-1959. Since 1958 men and machines had been driven at an exhausting pace with only secondary concern for cost, quality, and variety of output, maintenance of equipment, or morale of workers and party cadres. Trying to go too fast with too little, the regime had been unable to maintain balance in the economy. Machines were built without spare parts and factories were constructed without adequate transportation facilities. The size and scope of many construction projects were extended at local initiative without coordination with national plans. By mid-1960 abnormal numbers of machines were breaking down, many irrigation projects were ineffective, inventories of products of little economic use were mounting, and the people were becoming unable to maintain the frantic pace of the previous two years.

Economic and Political Effects of These Difficulties

20. The combined effect of two poor harvests, the withdrawal of Soviet technicians, and the failures of the "Leap Forward" has been sharply to reduce Communist China's rate of economic growth. Gross national product (GNP), which increased by about 18 percent in 1958 and 12 percent in 1959, is estimated to have increased by about 8 percent in 1960—approximately the average rate of increase during the First Five-Year Plan.¹ Output of crude steel, coal, and electric power apparently reached planned levels. However, industrial production increased by an estimated 18 percent against a planned increase of about 25 percent, and light industry registered little if any advance. Industries requiring a high level of technical skill, such as military industries, aircraft, shipbuilding, and atomic energy, probably encountered difficulties as a result of the withdrawal of Soviet technicians. Total investment is estimated to have remained at about the 1959 level, but investment in the industrial sector may have declined.

21. During the past three years Communist China has also encountered growing balance of payments problems. These problems—which arose out of the increased imports needed to support the attempted "Leap Forward" industrialization program and out of the necessity to cut back food exports—had their heaviest impact in 1960. The agricultural shortages probably caused total exports in the last half of 1960 to decline substantially.

22. Less tangible but equally important have been the political repercussions of China's economic difficulties. Despite three years of tremendous effort, the Chinese people face greater personal hardships today than when the "Leap Forward" with its grandiose promises began. Traditionally the Chinese have accepted hardship with considerable stoicism, and many older people, recalling mass starvation in the past, may credit the regime with preventing the situation from as yet deteriorating that far. However, under the commune system the Chinese state, rather than the family, has assumed the responsibility for providing food, and most Chinese probably place on the state the onus of responsibility for their present plight.

23. Moreover, the present food difficulties come atop vast social changes, exhausting labor pressures, policy vacillations, and unfulfilled promises. Present evidence suggests that large sections of the populace are disillusioned and apathetic and that confidence in the regime's policies has been badly shaken. Public morale, particularly in rural areas, is almost certainly at its lowest point since the Communists assumed power. Disaffection has in at least some instances taken the form of open dissidence, such as the appearance of antiregime wall posters, attacks on cadres, food riots, and various forms of sabotage of production. Nevertheless, we do not believe that widespread or organized efforts at rebellion or open rejection of the regime's authority are likely in the near future.

24. There is no indication that China's difficulties have caused the development of either severe factionalism within the leadership group or a challenge to Mao, although there almost certainly have been serious policy disagreements within the party. There is credible evidence that morale within the party has been shaken. The cadres have had to cope with the conflicting pressures of party orders, popular attitudes, and the often practical impossibilities of the given situation. Their task has been complicated by the problem of interpreting and implementing shifting policies without incurring subsequent

¹Prices of capital goods—the fastest growing sector of the economy—in China, where capital is scarce in comparison to labor, are high compared to prices of capital goods in the US. If they were valued in terms of the US price structure, the rate of growth of GNP would be slightly lower.

condemnation for "rightist" or "leftist" errors. The cadres probably are particularly resentful of the leadership's attempt to blame its failures on them. While the party almost certainly continues to be generally effective in maintaining order and discipline, we believe that its responses to the leadership are more sluggish and ill-coordinated.

25. Little is known about the attitudes of the regular military and public security forces. They have probably experienced some hardship along with the populace, even though they still receive preferential treatment. There have been reports of active discontent here and there among the security forces, but we have no basis for interpreting these reports as typical of the attitude of the security forces in general, much less that of the regular military forces.

III. THE REGIME'S REMEDIAL EFFORTS

26. The concern of Chinese Communist leaders over the food situation has been reflected in the emergency measures they have taken. Their major effort has been the adoption of a more rigorous rationing program both to equalize consumption throughout the country and to make sure that the limited food available is not consumed before the 1961 harvest.³ A cut in foodgrain rations averaging about 10 percent has been decreed to stretch available food supplies until the June harvests. Leaves have been ordered stripped from trees to be fed to animals so that food normally eaten by animals can be consumed by humans. The peasants have been permitted to have private plots once again, free markets have been allowed in at least some areas, and further modifications of the commune system have taken place. Regulations restricting food parcels from Hong Kong have been eased.

27. In addition to its efforts to stretch available supplies, the regime has taken steps to reduce the effects of the shortages. Medical

survey teams have been organized to check on malnutrition, and extra rations have been provided for the worst cases. In addition, Peiping has ordered the mobilization of all medical forces to fight an increase in infectious diseases expected this spring. The regime has also introduced measures to conserve the energies of the population, such as the elimination of many political meetings, the provision of extra rest days, and a suspension of organized sports. Extensive as these measures are, they appear to reflect grim determination rather than desperation on the part of the regime.

28. The most dramatic step taken by the regime—and perhaps the best indicator of the severity of the food shortage—is Peiping's decision to import several million tons of foodgrains. Under contracts already completed, imports of grain into China in 1961 will be nearly three million tons, most of which is scheduled for shipment in the first half of the year.

These imports are in sharp contrast to Communist China's normal trade pattern of net exports of over one million tons of grain. The following table illustrates this shift:

	Metric Tons 1959
MAJOR GRAIN IMPORTS (all from non-Bloc countries)	
Wheat (from Australia and Canada)	53,500
Barley (from Australia and Canada)
Rice (from Burma)	3,500
Rice (from Malaya) ...	7,000
Total Imports of Grain	64,000
ESTIMATED GRAIN EXPORTS:	
To Bloc countries	818,000
To non-Bloc countries ..	838,000
Total Exports of Grain	1,654,000
Estimated Net Exports (+) or Net Imports (-)	+1,590,000

³ While it is difficult for the regime to transfer grain from the rice-eating south to the wheat-eating north, it does have some room for maneuverability since rice can be substituted for wheat in central China, where both types of grain are consumed.

29. Agricultural exports have been the regime's chief means of paying for the imports necessary for its industrialization program. Imports of the amounts contracted for to date—which are to be paid for in cash—will cost Peking about \$200 million, and if negotiations now underway for additional grain are successful, total foodgrain imports in 1961 will cost over \$300 million. Whether or not the USSR has provided assistance to Peking for these purchases is unknown. In any event, Peking has increased its sales of silver bullion and has secured limited short-term credits from Hong Kong banks. In addition, it is seeking a six-month credit from Australia to cover future purchases. These measures will provide only a small part of the foreign exchange needed, however, and the major part will have to come from a cutback of industrial imports and a reduction of foreign exchange reserves.

30. Peking is also reorienting its domestic economic policies in an attempt to overcome the dislocations caused by the demise of the "Leap Forward" and the withdrawal of Soviet specialists. Although no details concerning a revised economic plan have been made public, statements on industrial policy indicate that scheduled rates of growth have been sharply reduced. The main effort in industrial construction for the next two or three years is apparently to be directed toward completing projects already begun. Quality and variety of output in industry is to receive greater attention than in the "Leap Forward" era. The rate of investment in heavy industry is to be reduced so that agriculture, light industry, mining, and transportation can catch up. If this policy is carried out, industrial investment may decline in 1961.

IV. FUTURE TRENDS

31. China's progress in overcoming its present economic difficulties will be primarily determined by the vagaries of weather and by developments in Sino-Soviet relations. Whether or not Soviet technicians return to China, we believe that the bitterness of the

Sino-Soviet dispute has caused the Chinese leaders to place increased importance on achieving self-sufficiency. Once having experienced the disruption caused by a sudden withdrawal of Soviet technicians, Peking is unlikely to allow itself to become so dependent on them in the future. Recent overtures to Italian and other Western European firms to send technical specialists to Communist China suggest that the Chinese are becoming more flexible in their willingness to use Western technicians.

32. China and the USSR are presently engaged in negotiations concerning future trade and economic relationships. We are not yet able to judge the likely outcome of these talks, but we believe that economic cooperation will not be as full as previously. Even if Soviet technicians return to China, the scope of their activities probably will be less than they were prior to mid-1960. In the absence of Soviet technicians the Chinese probably will concentrate on filling technological gaps as best they can in fields already partly developed—such as metallurgy, chemistry, and machine building—at the expense of more advanced industries.

33. While normal crop weather in 1961 would significantly improve farm output over the levels of 1959 and 1960, at least two years of average or better harvests will be required to overcome the crisis and permit a restoration of the diet to tolerable levels, some rebuilding of domestic stocks, and the resumption of net food exports. Over the longer term, the regime will be confronted with China's basic limitations on agricultural production, and will find it difficult to achieve increases in output commensurate with the rate of population growth. The regime appears to recognize this fact and to be reshaping its investment program to provide some additional resources for agricultural development. Although the regime will probably be able to secure the minimum essential growth in farm output, the margin over requirements will remain small owing to the basic aim of maximizing industrial expansion. In view of the vagaries of weather and the likelihood that the regime's predilection for "crash" programs

will prevent a steady and orderly agricultural development, agricultural crises probably will recur from time to time.

34. Communist China's current economic problems will also affect the amount and pattern of its foreign trade. Total exports in 1960 declined by about 10 to 15 percent below the high level of 1959 and may decline still further in 1961. China probably will be forced to request Bloc countries—chiefly the USSR—to defer the payments obligations it has incurred during recent years. Despite the strained relations between China and the USSR, we believe that Moscow will at least partially accede to such a request. Nevertheless, in view of China's reduced export capabilities and the large foodgrain imports from the West scheduled for 1961, imports of machinery and equipment—largely from the Bloc—may decline by as much as 30 percent compared to 1959 and 1960, and trade with the Free World may make up a significantly larger proportion of China's total trade.

35. Under these circumstances in industry, agriculture, and Sino-Soviet economic relations, GNP probably will increase by about 8 percent annually during the period 1961-1965—about the rate of increase during the First Five-Year Plan (1953-1957). On the assumption that Soviet technicians in large numbers do not return to China, industrial production is likely to increase about 12 percent annually, as compared with about 33 percent in 1959 and 18 percent in 1960. Only limited progress is likely in the more complex branches of industry, which will have a retarding effect on China's ability to produce a modern military establishment.

36. The economic difficulties confronting Communist China are unlikely to have a marked effect on Peiping's foreign policy. We believe that domestic difficulties will not, in themselves, either prompt Peiping to undertake a foreign adventure in order to divert domestic discontent or to refrain from such an adventure. Nor will present economic troubles significantly affect Communist China's aid commitments to Free World countries, since these involve only a minute part of Communist China's total output.

37. Peiping's recent failures, particularly its inability to solve the food problem, will almost certainly have some limiting effect on the impact and attraction of Communist China in Asia. Fear of and respect for Communist China will continue to be major factors in Asian politics. However, there is likely to develop—at least for the next few years—a less dazzled view of Communist China's economic achievements than has prevailed in recent years, especially since other Asian countries, such as Japan and India, have made relatively good economic progress during recent years.

V. THE CONTINGENCY OF POOR WEATHER IN 1961

38. Events so far have not been auspicious for this year's crops. The 1960 fall sowing was affected by drought, late harvest of summer crops, peasant apathy, and inadequate planning. As a result there apparently has been a reduction in winter crop acreage and generally late plantings. Below normal precipitation during the winter months in the North China plain—the major wheat area—has not provided favorable growing conditions for an area already short of soil moisture. However, if rainfall is adequate during the critical months of April and May a good wheat crop could still result. To date, precipitation and growing conditions in the rice producing areas of China have been about average.

39. A poor crop year in 1961, the third consecutive such year, would probably prevent any increase in GNP. China would be forced to reduce future industrial imports even more drastically than now appears necessary in order to continue or expand food imports. If industrial crops such as cotton and other fibers failed to recover, industry, chiefly light industry, would suffer in 1962, and the regime would have an extremely difficult time maintaining even the reduced pace of economic expansion it now appears to envisage.

40. Another poor crop would probably raise extremely grave problems for the regime in China. Unless there were substantial food imports, malnutrition and disease would become widespread and a considerable amount

of starvation would probably result. Party cohesion, effectiveness, and morale would drop. Public disaffection would probably become a major problem for the regime, and active resistance probably would occur, at least on a local level. If open resistance became widespread, the leadership would almost certainly undertake a massive campaign of threats and terror. While the responsiveness and effectiveness of its control apparatus would probably decline still further, it is unlikely that public disaffection would threaten the regime's control of China. Hunger and wide-scale passive resistance, however, would constitute acute economic and political problems for the Chinese Communist Party and China's development programs. We do not believe that even these difficulties would, in themselves, cause Peiping to engage in direct military aggression.

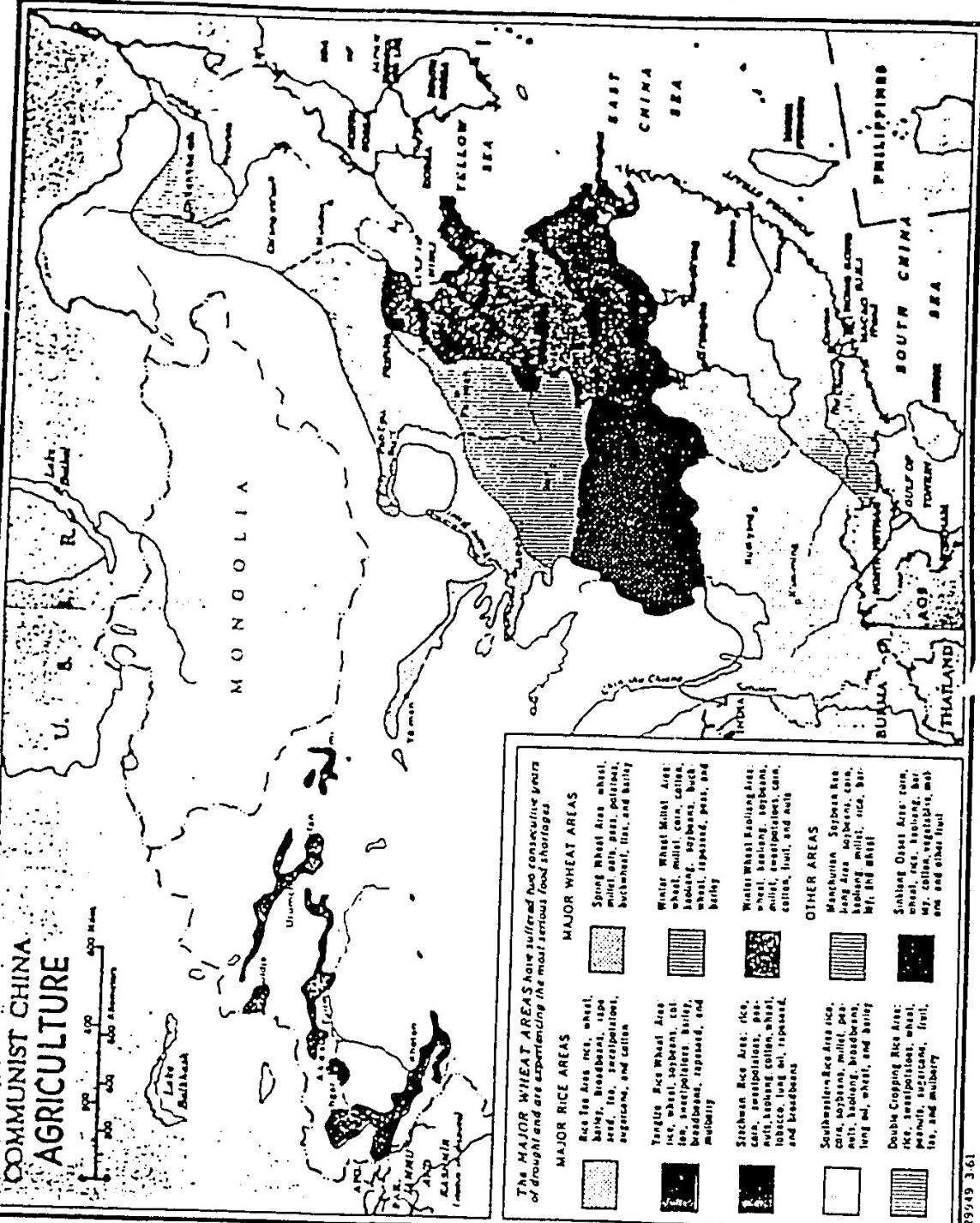
41. These circumstances probably would, however, prompt Peiping to avoid actions which would exacerbate its relations with Moscow. While China would be extremely reluctant to admit its inability to feed its people, the re-

gime probably would feel it could accept offers of food or other aid from another Communist country without too great a loss of face. Unless there is a further deterioration in Indo-Soviet relations, we believe that the Soviets would provide some assistance in such a time of crisis.

42. The regime has already made it clear that it will not accept food offers from the US in the present situation, and we believe that it will continue to take this position even if the 1961 crops are poor. The Chinese leaders probably will continue to take the line that China can overcome the present temporary difficulties by its own resources, that there is no famine, and that Westerners have, for ulterior motives, deliberately exaggerated the seriousness of the situation. Their principal consideration is, of course, a sense of national pride: acceptance of a food offer would be an admission that their own program had failed in an important respect, and, equally important, an acknowledgement that the West is genuinely interested in the welfare of the Chinese people.

COMMUNIST CHINA AGRICULTURE

400 Miles
0 100 200 300 400 Kilometers



THE MAJOR WHEAT AREAS have suffered two consecutive years of drought and are experiencing the most serious food shortages.

MAJOR RICE AREAS

Rice Irrigated Areas

rice, wheat, sorghum, corn, millet, barley, beans, cotton, oilseed, tea, vegetables, rapeseed, and mulberry

Rice Non-Irrigated Areas

wheat, millet, corn, cotton, barley, beans, rice, rapeseed, peas, and barley

Sichuan Rice Area

corn, beans, cotton, oilseed, tea, barley, and broadbeans

Southern Irrigated Area

corn, sorghum, millet, rice, barley, beans, cotton, oilseed, tea, barley, and broadbeans

Double Cropping Rice Area

rice, vegetables, wheat, peanuts, sugarcane, fruit, tea, and mulberry

MAJOR WHEAT AREAS

Spring Wheat Areas

wheat, millet, corn, cotton, oilseed, tea, rapeseed, and barley

Winter Wheat Areas

wheat, millet, corn, cotton, barley, beans, rice, rapeseed, peas, and barley

Winter Wheat Irrigated Areas

wheat, barley, corn, cotton, oilseed, tea, rapeseed, and barley

Other Areas

Manchuria, Szechuan, Kansu, Ninghsia, Shensi, Szechuan, Kansu, Ninghsia, and Shensi

Southern Other Areas

wheat, rice, vegetables, barley, corn, vegetables, meat, and other fruit